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The 'Failure to Mitigate' Defense in Antitrust

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The "failure to mitigate" defense in antitrust

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I. INTRODUCTION

Courts often state that antitrust plaintiffs have a duty to mitigate their damages.[1] But do they always? And when they do, what exactly is required? Courts have generally glossed over these questions, and scholarly commentary on the mitigation requirement is sparse.[2] This

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[1] *See, e.g.*, Fishman v. Estate of Wirtz, 807 F.2d 520, 558 (7th Cir. 1986); Pierce v. Ramsey Winch Co., 753 F.2d 416, 436 (5th Cir. 1985) ("Of course, an antitrust plaintiff, like other injured parties, must mitigate damages"); Malcolm v. Marathon Oil Co., 642 F.2d 845, 863 (5th Cir. Unit B Apr. 1981) ("[A]n antitrust victim must seek to minimize the amount of his damages"); Borger v. Yamaha Int'l Corp., 625 F.2d 390, 398–99 (2d Cir. 1980); Golf City, Inc. v. Wilson Sporting Goods Co., 555 F.2d 426, 436 (5th Cir. 1977) ("An antitrust plaintiff has a duty to mitigate damages"); Triebwasser & Katz v. AT&T Co., 535 F.2d 1356, 1360 (2d Cir. 1976) ("[I]t is apparent that the [antitrust] plaintiffs have an obligation to mitigate their damages"); Creative Copier Servs. v. Xerox Corp., 2005 WL 2175138, at *5 (D. Conn. Sept. 2, 2005); *In re* Visa Check/Mastermoney Antitrust Litig., 2003 WL 1712568, at *8 (E.D.N.Y. Apr. 1, 2003).

[2] Two law review articles address the mitigation requirement. *See* Amanda Kay Esquibel, *The Rule of Avoidable Consequences in Antitrust Cases: A*

article sets forth some guidelines concerning when courts should impose a mitigation duty—or, more precisely, when they should allow antitrust defendants to assert a "failure to mitigate" argument in order to reduce the amount of damages owed to plaintiffs who succeed in establishing liability.[3]

The article begins with the premise that any failure to mitigate defense should aim to minimize the sum of three costs: the costs associated with inefficient behavior by defendants, the costs associated with inefficient behavior by plaintiffs, and the administrative costs of claim adjudication. If cost minimization is the goal, then whether a failure to mitigate defense exists, and the content of the antitrust plaintiff's mitigation requirement, should differ depending on the type of damages the plaintiff is seeking to recover. The bulk of this article discusses how the defense should apply to different damages claims.

The article proceeds as follows: part II sets up the model by briefly outlining the three sources of social cost affected by recognition of a failure to mitigate defense and the three types of damages antitrust plaintiffs typically seek to recover. Parts III, IV, and V then consider how a failure to mitigate defense would affect the relevant social costs in each of the three damages contexts. I conclude that courts should not recognize a failure to mitigate defense when the antitrust plaintiff is seeking to recover overcharge damages but should do so when the plaintiff is seeking recovery of lost profits, even if the profit losses are the result of alleged market foreclosure.

Law and Economics Approach, 26 HOFSTRA L. REV. 891 (1998); Neil Hamilton & Virginia B. Cone, *Mitigation of Antitrust Damages*, 66 OR. L. REV. 339, 340 (1987). A third briefly addresses the duty to mitigate in connection with its consideration of how to value lost opportunities. *See* William B. Tye & Stephen H. Kalos, *Antitrust Damages from Lost Opportunities*, 41 ANTITRUST BULL. 637 (1996).

[3] The so-called duty to mitigate antitrust damages is not a true legal duty but is instead "a damages rule that limits damages that a plaintiff may recover." Esquibel, *supra* note 2, at 891. *See also Malcolm*, 642 F.2d at 863 n.30 (noting that "duty to mitigate" is actually rule of damage apportionment).

II. THE MODEL

Recognition of a failure to mitigate defense is likely to have different effects in different contexts. This article assumes that courts deciding whether to permit such a defense (and, if so, what it should consist of) should seek to minimize social costs. Accordingly, we begin by considering the types of costs a failure to mitigate defense may create or eliminate and the different contexts in which such a defense might be asserted. Parts III, IV, and V, then, will consider, context by context, the efficiency effects of recognizing a failure to mitigate defense.

A. The relevant social costs

A failure to mitigate defense denies antitrust plaintiffs the right to recover damages that they could have avoided using reasonable effort. Consistent with the normal proof burdens applicable in civil cases, the defendant bears the burden of proving both the fact that the plaintiff failed to use reasonable care to avoid damages and the quantum of claimed damages that could have been avoided had the plaintiff used such care.[4] The most obvious effect of recognizing a failure to mitigate defense, then, would be to alter the administrative costs—i.e., the sum of decision costs and error costs—associated with adjudicating antitrust claims. To the extent recognition of the defense simply adds inquiries to the process of ascertaining damages, it will tend to increase administrative costs. If, however, the defense somehow assists courts with the difficult task of sifting pro- from anticompetitive behavior, it may actually reduce administrative costs.

Recognition of a failure to mitigate defense is also likely to affect the behavior of the parties. Potential antitrust defendants may engage in more liability-creating behavior if they know they can reduce their expected penalties by invoking the failure to mitigate defense. And, of course, plaintiffs may act differently after an antitrust violation occurs if they know they will not be able to recover damages that they could have avoided using reasonable effort. Recognition of a failure to mitigate defense is therefore likely to alter (1) the administrative costs of adjudicating antitrust claims, (2) defendants' ex ante behavior (and the resulting social costs), and (3) plaintiffs' ex post behavior (and the

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4 *See, e.g., Malcolm*, 642 F.2d at 863.

resulting social costs). How the defense will affect these three categories of social cost will differ depending on the type of damages claim being asserted. Accordingly, we must consider the various types of damages private antitrust plaintiffs may seek to recover.

B. The types of private antitrust damages

In general, antitrust plaintiffs seek to recover damages for one of two types of injury. "Overcharge" injury consists of an overcharge or undercharge that the plaintiff suffers in its dealings with the defendant.[5] When the violation at issue is a conspiracy to fix prices above competitive levels, for example, the plaintiff's claim is that it had to pay more than it would have paid absent defendant's anticompetitive conduct—a literal overcharge. When the violation is a conspiracy among buyers to depress prices below competitive levels, the seller plaintiff claims that the buyer defendant paid less than it would have but for the anticompetitive behavior.[6] The distinguishing feature of overcharge claims is that the plaintiff is seeking to recover an economic benefit it lost in its dealings *directly with the defendant.*

The other main category of antitrust damages claims focuses on a business plaintiff's decreased profits.[7] A plaintiff asserting a "lost profits" claim ultimately emphasizes the degree to which its profits on business dealings *with others* were adversely impacted by the defendant's behavior. Thus, in a lost profits case, the plaintiff claims: "The profits I was able to secure from others were reduced by $*x* because of defendant's anticompetitive behavior."[8]

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[5] *See generally* HERBERT HOVENKAMP, FEDERAL ANTITRUST POLICY: THE LAW OF COMPETITION AND ITS PRACTICE 670–89 (3d ed. 2005) (cataloguing types of antitrust damage claims).

[6] As Professor Hovenkamp observes, "The term 'overcharge injury' may also describe the injury suffered by a seller for whom the price was suppressed by a monopsonist or buyer's cartel, or the injury suffered by the purchaser of an illegally tied product." *Id.* at 670.

[7] *Id.* at 678.

[8] *Id.* (observing that "[t]he basis of the loss may be a reduction in market share, a smaller markup per unit sold, an existing firm's loss of investment or business assets, or preclusion from entry into a profitable business").

Consumer plaintiffs, who normally do not suffer lost profits, generally seek to recover overcharges. Competitor plaintiffs, who normally do not purchase goods or services from their defendants, generally pursue lost profits. For plaintiffs who are businesses that utilize a defendant's products or services (i.e., business customers, rather than end-user consumers), the appropriate damages measure will likely depend on whether the defendant ultimately did conduct business with the plaintiff, albeit on noncompetitive price terms. If so, as when a business plaintiff bought an input from a defendant at a supracompetitive price resulting from horizontal price fixing, overcharge is probably the proper measure;[9] if not, as in a concerted refusal to deal case involving wrongful dealer termination, lost profits would likely be appropriate.[10]

Within the category of lost profits, there are a couple of subcategories: lost profits resulting from the increased costs occasioned by the defendant's conduct, and lost profits resulting from market foreclosure. The first subcategory would include, for example, the losses resulting when a supplier defendant engages in a concerted refusal to supply a plaintiff business with a necessary input, and the plaintiff has to utilize an inferior supply source (or is driven out of business).[11] The second would include, for instance, the lost business a competitor plaintiff suffers as a result of its defendant's exclusive dealing agreement.[12] Of course, this second subcategory is, to some degree, a subset

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[9] *But see* HERBERT HOVENKAMP, THE ANTITRUST ENTERPRISE: PRINCIPLE AND EXECUTION 73 (2005) (arguing for lost profits measure).

[10] If the product or service utilized by the plaintiff were available at a supracompetitive price, then the plaintiff could avoid losing profits by paying the amount of the overcharge. Because plaintiffs' damages (prior to trebling) would be the amount of the overcharge plus interest, cash-strapped plaintiffs could borrow the amount needed for the overcharge.

[11] *See, e.g.,* Malcolm v. Marathon Oil Co., 642 F.2d 845, 863 (5th Cir. Unit B Apr. 1981) (plaintiff claimed profit losses resulting from denial of input).

[12] *See, e.g.,* LePage's Inc. v. 3M, 324 F.3d 141, 157–60 (3d Cir. 2003) (en banc) (discussing plaintiff's exclusive dealing claims); United States v. Dentsply Int'l Inc., 399 F.3d 181 (3d Cir. 2005). While the plaintiff in *Dentsply* was the government, not a competitor seeking lost profits, the facts of the case nicely illustrate the theory of lost profits occasioned by market foreclosure.

of the first, for market foreclosure ultimately raises the cost of doing business by, for example, preventing the plaintiff from achieving economies of scale or relegating it to more costly distribution channels.[13] It is convenient, though, to draw a distinction between the "raised cost" and "foreclosure" subcategories of lost profits cases and to limit the former to those cases in which the plaintiff's costs are increased because of something other than market foreclosure.

Ultimately, then, we can identify three categories of antitrust damages: (1) losses from overcharges, (2) lost profits resulting from the increased costs occasioned by the defendant's behavior (typically, the denial of an input) but not relating to market foreclosure, and (3) lost profits resulting from market foreclosure. The remainder of this article details how the mitigation duty should vary, depending on the type of damages the plaintiff is seeking to recover.

III. THE DEFENSE IN OVERCHARGE CASES

We begin with the easiest context—overcharge injuries.[14] In theory at least, a plaintiff complaining of this sort of injury could mitigate his damages by purchasing the next-best product or service, as long as his welfare loss from utilizing that substitute would be less than the amount of the overcharge. Courts generally have not recognized a failure to mitigate defense in this context,[15] and for good reason: all three of the relevant social costs would increase if such a defense were permitted in this context.

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[13] *See, e.g.*, Einer Elhauge, *Defining Better Monopolization Standards*, 56 STAN. L. REV. 253, 321–22 (2003) (detailing how market foreclosure may raise rivals' costs).

[14] Recall that I am using the term "overcharge injury" to refer to all noncompetitive price injuries—both overcharges and undercharges. *See supra* note 6.

[15] *See, e.g., In re* Airline Ticket Comm'n Antitrust Litig., 918 F. Supp. 283, 286 (D. Minn. 1996) (denying mitigation defense when plaintiff sought undercharge damages occasioned by buyer cartel and observing that "[i]n a horizontal price-fixing case, . . . mitigation and offset generally do not affect the measure of damages"). Courts that have considered the issue have

A. Administrative costs

As explained in detail below, courts could ensure optimal deterrence of overcharge-creating conduct by setting overcharge damages equal to the amount of the overcharge plus any deadweight loss occasioned by the behavior at issue.[16] But that is not how they typically measure overcharge damages. Instead, they focus solely on the amount of overcharge.[17] More specifically, they measure overcharge damages by determining the difference between the price the plaintiff actually paid to the defendant (or received from the defendant, in an undercharge case) and that which he would have paid (or received) had the defendant not engaged in the anticompetitive behavior at issue.[18] This is a fairly straightforward inquiry. The price plaintiff paid or received is obviously easy to ascertain, and courts may determine the competitive price by utilizing either the "before-and-after" method, in which competitive price is deemed to be that which prevailed before and/or after the period of the defendant's anticompetitive behavior, or the "yardstick" method, in which the competitive price is determined based on the price of similar goods in markets not affected by the anticompetitive behavior at issue.[19]

Recognition of a failure to mitigate defense would substantially complicate this inquiry. Suppose, for example, that defendant's competitive price for a product was $100, the cartelized price was $125, and the value to plaintiff (i.e., his reservation price) was $130. Then

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cited the Supreme Court's decision in Hanover Shoe, Inc. v. United Shoe Machinery Corp., 392 U.S. 481 (1968), in support of their rejection of any failure to mitigate defense. *See, e.g., In re Airline Ticket Comm'n*, 918 F. Supp. at 286. While that seems to be an overly broad reading of *Hanover Shoe*, in which the Supreme Court refused to credit only one form of mitigation (i.e., passing the overcharge on to downstream customers), the holding that mitigation is not required in an overcharge case likely rests on solid policy grounds, as explained herein.

16 *See infra* notes 20–25 and accompanying text.

17 *See* HOVENKAMP, *supra* note 5, at 663–66.

18 *Id.* at 670–72.

19 *See id.* at 672–78 (discussing before-and-after and yardstick methods of measuring overcharge injuries).

suppose that a reasonable substitute product was available for $110 and would have produced $120 of value for plaintiff. If plaintiff bought defendant's product at the cartelized price ($125), he would receive $5 of surplus ($130 minus $125), which is $25 less than the surplus he would have received but for the anticompetitive conduct. If, however, plaintiff purchased the substitute product for $110, he would receive $10 of surplus ($120 minus $110), which is only $20 less than he would have received but for the anticompetitive conduct. He could thus mitigate his loss by $5 by engaging in a substitute transaction. But, of course, it would be next to impossible for any court to figure this out. Determining what constitutes the most reasonable substitute from a plaintiff's perspective would amount to guesswork, and reservation prices are almost incapable of proof. A failure to mitigate defense would therefore involve the parties in expensive and ultimately insoluble proof disputes that would raise administrative costs substantially.

B. Costs resulting from defendant behavior

Recognition of a failure to mitigate defense in this context would also increase the social costs resulting from inefficient behavior by defendants. To see why this is so, consider the aforementioned "optimal deterrence" model of antitrust damages. Assuming that the sole purpose of damage-trebling is to account for the likelihood that violations will not be successfully detected and prosecuted (in other words, that the probability of detection and successful prosecution is precisely one-in-three), that model seeks to set base (pretrebled) overcharge damages so that they exceed the defendant's gain from engaging in the conduct at issue when the conduct involves a social loss, but do not do so when the conduct enhances total social wealth—i.e., is Kaldor-Hicks efficient.[20] If base damages are so determined, defendants will be incentivized to engage in efficient conduct but to avoid inefficient conduct.[21]

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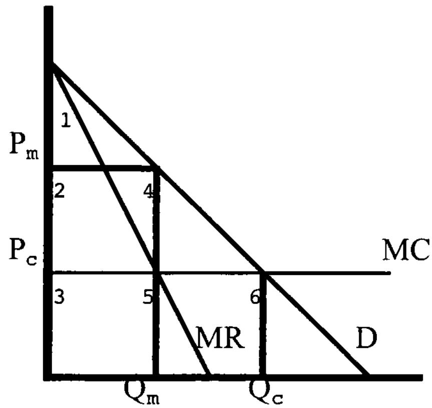
[20] *See id.* at 657–63 (discussing optimal deterrence model of antitrust damages).

[21] The optimal deterrence model assumes that efficiency, not victim compensation, is the goal of the antitrust damages determination.

In light of this ultimate goal, the optimal deterrence model concludes that the base damages amount in overcharge cases should equal the amount of the overcharge (square 2-3-5-4 in the standard monopoly pricing model depicted in the figure) plus the deadweight loss occasioned by defendant's anticompetitive conduct (triangle 4-5-6 in the figure).[22]

Figure
The Monopoly Pricing Model



D =	Demand	Q_m =	Monopoly Output
MC =	Marginal Cost	Q_c =	Competitive Output
MR =	Marginal Revenue	P_m =	Monopoly Price
		P_c =	Competitive Price

22 The figure diagrams the result of an exercise of market power. In perfect competition, the seller maximizes his returns by producing Q_c units and charging a price of P_c. When the seller has market power as a result of either monopoly or collusion, he maximizes his return by lowering output to Q_m and charging a price of P_m. This has two primary effects: first, wealth is transferred from consumers to the seller, who is now charging higher per-unit prices; second, some consumers (those located from points 4 to 6 on the demand curve) substitute away from the seller's product to what would have been their second choice in a competitive market. This inefficient substitution is generally referred to as "deadweight loss," a term that should also include the costs of preventing exercises of market power and enforcing laws against such exercise.

A damages rule requiring the defendant to pay only the deadweight loss occasioned by its anticompetitive conduct would underdeter, for deadweight loss will typically be less than the amount of wealth transfer from consumers to defendants, and defendants will therefore continue to engage in inefficient, anticompetitive practices if they must simply pay an amount equal to the social cost of their activity.[23] By the same token, a damages rule requiring merely the disgorgement of the overcharge would underdeter when the conduct at issue increased the defendant's efficiency, but by less than the amount of deadweight loss occasioned by the practice.[24] Consider, for example, a competitor collaboration that increased a defendant's efficiency by $200 but created market power that transferred $1000 worth of surplus from consumers to the defendant and generated $500 worth of deadweight loss. A damages rule that merely required disgorgement of overcharge would not deter this practice (the defendant would get $1200 in benefit and would only have to pay $1000), even though the practice would result in a net social loss of $300 ($500 deadweight loss minus $200 efficiency gain).

If the measure of damages in overcharge cases is set to equal the amount of overcharge plus the deadweight loss, optimal deterrence will be achieved. Practices that create both efficiencies and market power will be pursued only if the efficiencies created exceed the social loss occasioned by the practice, i.e., only if the practice at issue is Kaldor-Hicks efficient.[25] For practices that create no efficiencies,

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[23] If, for example, a practice transferred $1000 from consumers to defendants and produced $500 in social loss, a rule requiring the defendant to pay merely the social cost of his conduct ($500) would not motivate him to forgo the cost-creating activity. To deter the conduct at issue, damages would have to be at least $1000, the amount by which the conduct benefits the defendant.

[24] *See* HOVENKAMP, *supra* note 5, at 660.

[25] For example, this damages rule would deter a competitor collaboration that increased defendant's efficiency by $200 but created market power that transferred $1000 worth of surplus from consumers to the defendant and generated deadweight loss of $500. While the collaboration would create $1200 of benefit for the defendant, the damages rule would require him to pay $1500, so he would not engage in the collaboration.

such as naked price fixing, the damages award is likely to be larger than necessary to motivate efficient behavior (simple overcharge disgorgement would suffice), but overdeterrence is not a concern in such cases.

Of course, the optimal deterrence model bears little resemblance to the damages measure courts normally utilize in overcharge cases. As noted above, courts typically measure overcharge damages by the difference between the price actually paid to the defendant[26] and that which would have prevailed under competitive conditions.[27] In other words, courts have generally ignored deadweight loss, which is notoriously difficult to measure, and have simply awarded the amount of the overcharge.

The optimal deterrence model indicates that this measure is underdeterrent in cases in which the illegal conduct creates some efficiencies for the defendant.[28] Recognition of a failure to mitigate defense would render the measure similarly underdeterrent even when the conduct at issue creates no such efficiencies. Consider, for example, a naked price-fixing conspiracy that involves no efficiencies whatsoever and results in a transfer of $1000 from consumers to producers and a deadweight loss of $500. If the plaintiffs' expected damages were at least $1000, this conspiracy (which reduces social welfare by $500) should be deterred. Suppose, though, that the defendant could show that the plaintiffs could have mitigated their surplus loss by $100 by purchasing a substitute product from another seller. If a failure to mitigate defense reduced plaintiffs' expected damages award to $900, then the conspiracy would not be deterred, for the defendant would expect to earn $1000 from conduct that would create liability of only $900. Thus, recognizing a failure to mitigate defense to a claim of overcharge damages would likely exacerbate the underdeterrence problem inherent in courts' standard measure of overcharge damages and would thereby increase the social costs resulting from inefficient behavior by defendants.

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26 Or, in a monopsony undercharge case, collected by the plaintiff.

27 *See supra* notes 17–19 and accompanying text.

28 *See supra* note 24 and accompanying text.

C. Costs resulting from plaintiff behavior

But what about the effect of a mitigation defense on the behavior of plaintiffs? In tort and contract law, the failure to mitigate defense is generally aimed at ensuring efficient conduct by the victim.[29] Specifically, the law aims to incentivize plaintiffs to make the substitutions necessary to ensure that resources are put to their highest and best use.[30] When it comes to antitrust plaintiffs claiming overcharge damages, though, any substitution by the victim plaintiff in response to a violation would likely be inefficient.

To see why this is so, consider the welfare effects plaintiffs' substitution away from defendants' supracompetitively priced products would have on the parties themselves and on third parties. Such substitution creates no value for a plaintiff, for whom the substituted product is a second-best option. If the plaintiff is compensated for the welfare loss he experiences because of the substitution, then he will not be worse off for having substituted, but the substitution itself creates no real value for the plaintiff. Nor would such substitution create value for the defendant. He may benefit if, under the governing legal rule, the substitution reduces the magnitude of the plaintiff's damage award, but in that event, it is the legal rule, not the plaintiff's substitution, that creates value for the defendant. There is no independent reason for the defendant to prefer substitution; indeed, the defendant would likely prefer that the plaintiff not substitute.

Finally, the net third-party effect of substitution by the plaintiff would be negative. While plaintiff substitution would create some "winners" (e.g., suppliers of the substituted products) and some "losers" (e.g., customers of the plaintiff, who will suffer if the substi-

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[29] *See, e.g.*, Outboard Marine Corp. v. Babcock Indus., Inc., 106 F.3d 182, 184 (7th Cir. 1997) (Posner, J.) (observing that the doctrines of mitigation of damages in contract law and avoidable consequences in tort law "are primarily concerned with efforts by victims of a breach of contract or a tort, exerted after the breach or tort has occurred, to minimize the harm").

[30] So, for example, if a buyer were to renege on its promise to purchase a bridge the seller was constructing, the failure to mitigate defense would encourage the seller to stop work on the bridge and to reallocate its productive resources (labor, materials, etc.) to substitute projects. *See* Rockingham County v. Luten Bridge Co., 35 F.2d 301 (4th Cir. 1929).

tuted input is inferior), the losses to losers would exceed the gains to winners. Prior to defendant's actions that artificially reduced output and thereby occasioned the overcharge, resources were efficiently allocated by having the plaintiff buy from the defendant. If a substitution were efficient, the plaintiff would have made it, for any beneficiaries from such substitution would have offered enough to compensate any victims. Thus, we can confidently predict that the positive third-party effects resulting from post-violation substitution would be less than the negative third-party effects; otherwise, such substitution would have occurred prior to the violation.

In short, any substitution by the plaintiff would be, on the whole, inefficient and should not be encouraged. Indeed, such inefficient substitution is the primary component of the deadweight loss that results from monopoly pricing.[31] Obviously, optimal deterrence would not be achieved if an increase in deadweight loss (from increased substitution) resulted in a *reduction* of defendant's penalty. It appears, then, that all three of the relevant social costs would increase if a failure to mitigate defense were recognized in overcharge cases.

IV. THE DEFENSE WHEN PLAINTIFF SEEKS PROFIT LOSSES RESULTING FROM DENIAL OF AN INPUT

In our second category of antitrust damages, the plaintiff is not claiming that he paid a supracompetitive price for the defendant's product or service (either as an end-user consumer or as a business that utilizes the product or service as an input) but that he was denied that product or service altogether and therefore lost profits that he otherwise would have earned. This damages measure therefore applies to cases in which the plaintiff (1) is a profit-seeking entity, not an individual consumer, (2) utilizes the defendant's product or service as an input, and (3) could not have obtained the input from the defendant by paying a supracompetitive price.[32] Wrongful dealer ter-

[31] *See supra* note 22.

[32] If the plaintiff could have obtained the input by paying the defendant a supracompetitive price, the proper measure of damages is overcharge. *See supra* note 10 and accompanying text.

mination cases, for example, fall into this category. The key mitigation question presented in this context is whether the defendant may reduce the amount of damages owed to the plaintiff by proving that the plaintiff failed to take reasonable steps to find a substitute for the defendant's product or service.

Courts have provided different answers to that question. In the majority of cases in which the issue has been squarely presented, the court has recognized a failure to mitigate defense.[33] Representative of this group of cases is *Borger v. Yamaha International Corp.*,[34] in which the plaintiff, a distributor of audio products, was terminated as a dealer and accused the defendant manufacturer of a concerted refusal to deal. Finding the defendant liable, the jury awarded damages to the plaintiff based on an instruction stating that the proper measure of damages was the lost profits the plaintiff would have earned from the dealership had it received it.[35] The Second Circuit reversed on grounds that plaintiff's "duty to mitigate" required it to take reasonable steps to merchandise substitute lines, so any profits that could have been generated by those efforts must be subtracted from plaintiff's damages.[36] By contrast, the Fifth Circuit recently denied a mitigation defense to a clothing manufacturer charged with terminating a dealer as part of a vertical resale price maintenance conspiracy. In *PSKS, Inc. v. Leegin Creative Leather Products, Inc.*,[37] the Fifth Circuit held that profits the terminated dealer could have earned by selling substitute products did not have to be deducted from the dealer's damages.[38] Similarly, in

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[33] *See, e.g.*, Pierce v. Ramsey Winch Co., 753 F.2d 416 (5th Cir. 1985); Malcolm v. Marathon Oil Co., 642 F.2d 845 (5th Cir. Unit B Apr. 1981); Borger v. Yamaha Int'l Corp., 625 F.2d 390 (2d Cir. 1980); Golf City, Inc. v. Wilson Sporting Goods Co., 555 F.2d 426 (5th Cir. 1977); Creative Copier Servs. v. Xerox Corp., 2005 WL 2175138 (D. Conn. Sept. 2, 2005); Westman Comm'n Co. v. Hobart Corp., 541 F. Supp. 307, 314 (D. Colo. 1982).

[34] 625 F.2d 390.

[35] *Id.* at 398–99.

[36] *Id.* at 399.

[37] 2006 WL 690946 (5th Cir. Mar. 20, 2006), mandate stayed pending filing and disposition of petition for writ of certiorari, 2006 WL 2466835 (U.S. Aug. 28, 2006).

[38] *PSKS*, 2006 WL 690946 at *5.

Trabert & Hoeffer, Inc. v. Piaget Watch Corp.,[39] the Seventh Circuit refused to credit the defendants' argument that the plaintiff jewelry retailer, who claimed to have been terminated as part of a vertical price-fixing conspiracy among the defendants, could have avoided losses altogether by selling substitute watches.[40]

The relevant question here, of course, is whether courts *should* recognize a failure to mitigate defense that effectively saddles "denial of input" plaintiffs with an obligation to seek out alternative sources of supply. To answer that question, we return to our three sources of social cost. Recognition of a failure to mitigate defense increases the administrative costs of determining plaintiffs' damages, but that cost increase is likely outweighed by cost savings from more efficient behavior by plaintiffs and defendants.

A. *Administrative costs*

Absent a mitigation defense, an antitrust tribunal would normally determine a plaintiff's lost profits by using either the familiar before-and-after method, in which the court compares the plaintiff's profits during the period of defendant's anticompetitive conduct with its profits before and/or after that conduct ends, or the yardstick method, in which the court compares the plaintiff's profits in the market affected by the defendant's conduct with profits of similarly situated entities in other markets.[41] A failure to mitigate defense would require courts to make additional findings regarding what constitutes "reasonable" mitigation efforts on the part of the plaintiff and what quantum of plaintiff's alleged damages could have been avoided had plaintiff engaged in such efforts. Recognition of the defense would therefore raise the cost of determining damages in denial of input cases. But those increased costs are likely offset by cost savings resulting from the salutary incentives created by the defense.

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[39] 633 F.2d 477 (7th Cir. 1980).

[40] Note that the issue in *Trabert* was whether, given the mitigation possibility, the plaintiff had established the *fact* (not the amount) of damages. *See id.* at 482.

[41] *See* HOVENKAMP, *supra* note 5, at 680–83 (describing before-and-after and yardstick methods for calculating lost profits).

B. Costs resulting from plaintiff behavior

First, a failure to mitigate defense reduces the costs associated with inefficient plaintiff behavior by encouraging plaintiffs to make efficient use of productive resources.[42] Consider, for example, a retailer that has been wrongfully terminated as a dealer for a defendant manufacturer. Social welfare would be enhanced if the retailer were to fill the shelf space previously devoted to the defendant's products with substitute merchandise, and the damages rule should therefore encourage such replacement. A rule denying damages that could have been avoided using reasonable efforts would provide such an incentive. Suppose, for example, that the clothing retailer plaintiff in the Fifth Circuit's recent *PSKS* case[43] would have lost $10,000 in profits due to the loss of defendant's clothing line but could have made $5000 by filling its empty shelf space with other competing lines of clothing. If the plaintiff were permitted to recover its full, unmitigated profit loss (as it was under the Fifth Circuit's ruling), then it would have no incentive to restock the shelves with competing merchandise. If, however, the rule were that plaintiff's damages must be reduced by the amount of profit it could have earned retailing the next-best clothing line ($5000 in our hypothetical), then the plaintiff would be encouraged to restock its shelves. It would reason that if it left the shelves barren, it would end up with $5000 total, but if it sold the best alternative line, it would end up with $10,000 ($5000 in damages and $5000 profit from alternative sales). A failure to mitigate defense, then, would encourage efficient resource allocation by plaintiffs.

C. Costs resulting from defendant behavior

But what about the effect of the defense on defendants' incentives? Wouldn't such a defense decrease defendants' expected penalties and thereby reduce their disincentive to engage in the sort of

[42] *See* Hamilton & Cone, *supra* note 2, at 368 (observing that "[r]esources are not efficiently allocated if antitrust plaintiffs do not undertake reasonable steps to put their resources to work in readily available, cost-effective alternatives").

[43] PSKS, Inc. v. Leegin Creative Leather Prods., Inc., 2006 WL 690646 (5th Cir. Mar. 20, 2006), mandate stayed pending filing and disposition of petition for writ of certiorari, 2006 WL 2466835 (U.S. Aug. 28, 2006).

conduct that gives rise to denial of input claims? Almost certainly, yes. But that's probably a good thing. Conduct that results in denial of input claims is likely to be overdeterred by substantive antitrust doctrine, so a doctrine that limits damages based on such claims likely has a desirable effect on defendants' incentives.

Claims for profit losses resulting from the denial of an input commonly arise in connection with allegations that a defendant manufacturer has terminated a plaintiff dealer pursuant to a conspiracy involving vertical resale price maintenance (VRPM).[44] Because minimum VRPM is per se illegal under the antitrust laws,[45] a plaintiff that convinces a jury that the defendant has engaged in such conduct is automatically entitled to treble damages, even if the plaintiff can demonstrate no anticompetitive effect. This outcome is troubling for at least two reasons. First, many instances of VRPM are efficient (primarily because such price maintenance provides a means of overcoming the free-rider problem that inheres in any business involving networks of dealers),[46] and a rule of automatic liability is therefore overinclusive. Second, VRPM—unlike, say, horizontal price fixing, predatory pricing, and improper patent infringement suits—is not a "hidden" antitrust violation that might not be detected by a potential plaintiff. The generally accepted rationale for trebling is that antitrust violations are difficult to detect, so that a rule providing only single damages would make such violations profitable and would thus underdeter.[47] Because technical antitrust violations arising from

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[44] *See, e.g.*, Beach v. Viking Sewing Mach. Co., 784 F.2d 746 (6th Cir. 1986); Pierce v. Ramsey Winch Co., 753 F.2d 416 (5th Cir. 1985); Borger v. Yamaha Int'l Corp., 625 F.2d 390 (2d Cir. 1980); *PSKS*, 2006 WL 690646.

[45] *See* Dr. Miles Med. Co. v. John D. Park & Sons Co., 220 U.S. 373, 400 (1911). *See also* Simpson v. Union Oil Co. of Cal., 377 U.S. 13, 17 (1964) ("[A] supplier may not use coercion on its retail outlets to achieve resale price maintenance"); United States v. Parke, Davis & Co., 362 U.S. 29, 44 (1960) (reiterating rule against minimum VRPM). Note that the U.S. Supreme Court stayed the mandate in the Fifth Circuit's PSKS case, thereby signalling that it may revisit the per se rule against VRPM. *PSKS*, 2006 WL 2466835.

[46] *See generally* HOVENKAMP, *supra* note 5, at 456–64.

[47] *Id.* at 666.

VRPM (and imposition of vertical nonprice restraints) are almost sure to be detected and usually will not lead to anticompetitive harm, current law is likely overdeterrent.[48] Accordingly, reducing defendants' expected penalties by recognizing a failure to mitigate defense in denial of input cases likely pushes defendants' incentives in the right direction, i.e., toward optimal deterrence.[49]

V. THE DEFENSE WHEN PLAINTIFF SEEKS PROFIT LOSSES STEMMING FROM MARKET FORECLOSURE

Finally, we come to the most difficult context—that in which the plaintiff is claiming damages for profit losses occasioned by its foreclosure from the market. This context differs from the previous one in that the plaintiff is complaining that the defendant denied it a marketing opportunity, not a productive input of some sort. This category will generally include cases involving exclusive dealing,[50] tying,[51] and "purchase target" discounts, e.g., loyalty rebates or bundled discounts.[52]

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[48] For a persuasive proposal to confine damages-trebling to "clandestine" antitrust violations, *see* HOVENKAMP, *supra* note 9, at 66–68.

[49] Of course, if the denial of input results from a manufacturer-dealer conspiracy that is not designed to maintain resale prices or impose nonprice restraints but is instead aimed at eliminating the dealer's competitor(s), *see, e.g.*, Westman Comm'n Co. v. Hobart Corp., 541 F. Supp. 307 (D. Colo. 1982) (denial of input case in which plaintiff alleged this sort of conspiracy), the substantive law of antitrust is probably not overdeterrent, and recognition of a failure to mitigate defense may have an undesirable effect on the incentives of potential defendants. A review of the reported cases suggests, though, that this sort of denial of input case is rare and that most involve allegations of VRPM or manufacturer imposition of nonprice restraints.

[50] Exclusive dealing may result in market foreclosure because the defendant contractually bars customers from purchasing the plaintiff's wares. *See* HOVENKAMP, *supra* note 5, at 436–37.

[51] Tying defendants require purchasers of their monopoly tying products to purchase their tied products as well, thereby foreclosing competing sellers in the tied product market. *See id.* at 423–24.

[52] "Purchase target" discounts, which reward customers who purchase more of their requirements from the discounter, tend to take business from the discounter's rivals. *See generally* Willard K. Tom, David A. Balto, & Neil

Mitigation in this context would consist of reasonable efforts by the plaintiff to sell its products or services elsewhere. It would be only reasonable, for example, for the operator of a moveable hot dog stand who found himself "foreclosed" from his original Manhattan street corner to seek out another street corner on which to sell his wares. Indeed, his selection of the original street corner involved an opportunity cost in the form of the forgone profits from selling on the next-best street corner, so his "foreclosure" from his original corner might be viewed as eliminating that cost. In a lawsuit based on his foreclosure from the original street corner, the opportunity cost eliminated by the foreclosure would have to be deducted from the vendor's damages.[53]

What constitutes reasonable efforts to sell elsewhere will, of course, differ from case to case. At a minimum, reasonable efforts would seem to include searching for alternative markets and lowering one's price to the level of marginal cost. In addition, a foreclosed competitor should complain directly to the defendant about the foreclosure at issue. In many cases, the small competitors most likely to be foreclosed by a defendant's marketing practices (and most likely to make sympathetic antitrust plaintiffs) are not the target of the defendant's strategic behavior and would be granted relief if it were requested.[54] A foreclosed plaintiff might also mitigate its profit losses

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W. Averitt, *Anticompetitive Aspects of Market-Share Discounts and Other Incentives to Exclusive Dealing*, 67 ANTITRUST L. J. 615, 622–29 (2000). Purchase target discounts may be structured as single-product loyalty discounts (or rebates) or as "bundled" discounts (or rebates), in which the discount/rebate is conditioned upon purchasing products from multiple product markets. *See generally* Thomas A. Lambert, *Evaluating Bundled Discounts*, 89 MINN. L. REV. 1688, 1693–99 (2005) (cataloguing the types of purchase target discounts and summarizing arguments as to why they may raise competitive concerns).

53 Tye & Kalos, *supra* note 2, at 646 ("Lost net revenues do not represent true damages in this case because the lost revenues are offset by opportunity costs of an equal amount. In legal parlance, it may be said that the foreclosed competitor could have mitigated damages by the amount of opportunity costs"). *See also* Fishman v. Estate of Wirtz, 807 F.2d 520, 556–58 (7th Cir. 1986) (holding that opportunity cost should be deducted from award of antitrust damages).

54 For example, Johnson & Johnson, Inc. ("J&J") was recently sued over market foreclosure resulting from bundled discounts it provided on packages of sutures (surgical stitches) and trocars (devices used in endoscopic surgery).

by altering its business model. As Professor Crane has observed, a plaintiff foreclosed by a bundled discount that covers products he does not sell could seek to collaborate with other sellers of those products to offer a competing bundle.[55] And a competitor plaintiff in any type of foreclosure case (tying, exclusive dealing, or exclusionary discounts) could mitigate by seeking to become a supplier to the defendant. If the plaintiff were at least as efficient a producer as the defendant, both parties would be better off if the defendant purchased the products or services at issue from the plaintiff rather than produced them itself.[56] Defendants, then, would likely accept good faith supplier offers from equally (or more) efficient rivals, permitting those rivals to continue selling their wares.[57]

The plaintiff, a small manufacturer of trocars, claimed that J&J's discounts anticompetitively foreclosed it from the trocar market, for it did not manufacture sutures and thus could not offer a competitive package discount. On a motion for summary judgment, J&J successfully argued that it had responded to the plaintiff's complaints about foreclosure by "carving out" plaintiff's products so that customers who purchased plaintiff's products could still qualify for J&J's discounts. *See Order Granting in Part and Denying in Part Defendant's Motion for Summary Judgment*, Applied Medical Resources Corp. v. Ethicon Inc., No. 03-CV-1329 (C.D. Cal. Feb. 2, 2006) (copy on file with author). The target of J&J's bundled discounts, it seems, was not plaintiff but Tyco Corp., which manufactures both sutures and trocars and was engaging in consumer-friendly bundle-to-bundle competition with J&J. *Id.* at 3. The plaintiff was thus able to mitigate its damages by complaining directly to J&J.

[55] *See* Daniel A. Crane, *Multiproduct Discounting: A Myth of Nonprice Predation*, 72 U. CHI. L. REV. 27, 31–32 (2005). *See also* Lambert, *supra* note 52, at 1746–47 (noting same mitigation possibility).

[56] *See* E. THOMAS SULLIVAN & JEFFREY L. HARRISON, UNDERSTANDING ANTITRUST AND ITS ECONOMIC IMPLICATIONS 184 (1994) (noting that "greater efficiency is an ideal way to overcome an 'entry barrier,'" for the more efficient, but foreclosed, rival may begin supplying the competitor responsible for the foreclosure); ROGER D. BLAIR & DAVID L. KASERMAN, ANTITRUST ECONOMICS 403–04 (1985) (observing that monopolist engaged in tying would purchase tied product from more efficient rivals).

[57] For an example of how supplier arrangements have been used to mitigate the market foreclosure resulting from a rival's efficient business practice, consider the experience of small regional airlines that in recent years have found themselves foreclosed from the markets for their routes because of a form of bundled discounts offered by the major air carriers. Major carriers charge far

Having considered how a plaintiff claiming profit losses from market foreclosure might mitigate its damages, we turn to consider how recognition of a failure to mitigate defense in this context would affect the three relevant social costs.

A. *Administrative costs*

Whereas a failure to mitigate defense would likely increase administrative costs in the other two damages categories, recognition of the defense in this context could actually reduce the costs of claim adjudication by reducing error costs.[58] To see why this is so, consider (1) the challenge facing courts tasked with adjudicating foreclosure-based lost profits claims and (2) how a failure to mitigate defense could assist courts with that task.

1. THE CHALLENGE FOR COURTS The practices for which market foreclosure plaintiffs seek to recover lost profits are, from a competitive standpoint, "mixed bags" that may create both pro-competitive benefits and anticompetitive costs. Tying, originally condemned under the now-discredited leverage theory,[59] may harm

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less for a bundle of flights going from departure point to hub to destination than they would for two single flights, one from departure point to hub and another from hub to destination. Small carriers that service only one leg of this sort of journey tend to be foreclosed by such pricing, for they cannot compete unless they offer the entire amount of the bundled discount on the leg they service, and doing so would require them to price below cost. The regional airlines, however, have not been driven out of business by the major carriers' bundled discounts but have instead remained in business (and have thrived, in fact) by becoming suppliers to the major carriers. *See* Eric Wieffering, *Engine of Change*, STAR TRIB. (Minneapolis), May 11, 2003, at 1D (documenting successful supply relationships between small regional and major air carriers).

[58] The administrative costs of claim adjudication include both decision costs (the cost of making the decision) and error costs (the cost of mistakes).

[59] Under the leverage theory, a seller with a monopoly in one product employs tying to create a limited monopoly in a second "tied" product that is essential to the use of the first "tying" product. *See, e.g.*, Carbice Corp. of Am. v. Am. Patents Dev. Corp., 283 U.S. 27, 31–32 (1931) (articulating leverage theory). The leverage theory has been largely discredited by the Chicago school's observation that when two components are used in conjunction with one another, there is only one final product, and, thus, only one monopoly

competition if it is used to raise rivals' costs (by reducing their market share and, consequently, their economies of scale), facilitate collusion or oligopoly pricing, or create entry barriers.[60] On the other hand, tying may increase output by metering demand and facilitating price discrimination among consumers.[61] Exclusive dealing arrangements may raise the costs of rivals by relegating them to inferior distribution channels or by preventing them from attaining economies of scale,[62] but such arrangements may also provide more efficient means of allocating resources than either vertical integration or unfettered markets.[63] Similarly, single-product loyalty discounts may raise rivals' costs if they permit the discounter to attain enough market share to prevent rivals from attaining economies of scale,[64] and bundled discounts may exclude efficient competitors that sell a narrower line of products than the discounter,[65] but both forms of discounting result in lower prices that generally benefit consumers and may reflect scale and/or scope economies.[66] Accordingly, it is often difficult for courts to determine whether foreclosure-causing practices are, on the whole, output-

power to be exploited. *See, e.g.*, Ward S. Bowman, Jr., *Tying Arrangements and the Leverage Problem*, 67 YALE L. J. 19 (1957).

[60] *See* HOVENKAMP, *supra* note 5, at 420–25. Tying may also be used to evade rate regulation. Such evasion may or may not be anticompetitive (depending on the competitive effect of the regulation itself) and should probably be challenged under the law of the relevant regulatory regime, not under antitrust law. *See id.* at 425–27.

[61] *See id.* at 428–30.

[62] *See id.* at 436–37.

[63] *See id.* at 439–41.

[64] *See* Tom, et al., *supra* note 52, at 622–27.

[65] *See* LePage's Inc. v. 3M, 324 F.3d 141, 155 (3d Cir. 2003) (en banc) ("The principle anticompetitive effect of bundled rebates is that when offered by a monopolist they may foreclose portions of the market to a potential competitor who does not manufacture an equally diverse group of products and who therefore cannot make a comparable offer").

[66] *See* Daniel A. Crane, *Mixed Bundling, Profit Sacrifice, and Consumer Welfare*, 55 EMORY L. J. 423 (2006); Lambert, *supra* note 52, at 1723–24.

enhancing (in which case they should be permitted) or anticompetitive (in which case they should be condemned).[67]

That difficulty is exacerbated by the fact that plaintiffs challenging foreclosure-causing practices are not seeking to recover the social costs occasioned by defendants' conduct but are instead focused on recouping their own lost profits. Plaintiffs who find their profits reduced because of foreclosure will therefore sue even if the foreclosure-causing practice is entirely efficient. And, because there is likely no useful correlation between the deadweight loss occasioned by a defendant's foreclosure-causing practice and the amount of any competitor plaintiff's lost profits, the evidentiary record in a case where the plaintiff is seeking to recover lost profits from foreclosure is unlikely to assist the court in segregating procompetitive from anticompetitive practices.[68] One solution to this problem would be to eliminate competitor lawsuits based on market foreclosure and to rely entirely on consumer overcharge suits, which would be filed only if the foreclosure-causing practice at issue actually resulted in increased prices.[69] But, as Professor Hovenkamp has argued, eliminating foreclosure-based lost profits actions by competitors would eliminate an

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[67] *See* Frank H. Easterbrook, *When Is It Worthwhile to Use Courts to Search for Exclusionary Conduct?*, 2003 COLUM. BUS. L. REV. 345, 345 (describing difficulty confronting courts seeking to distinguish competitive from exclusionary conduct).

[68] Professor Hovenkamp explains:

> [T]here is probably no useful correlation between the amount of an injured competitor's lost profits and other consequential damages, and the amount of the monopoly overcharge and deadweight loss caused by the defendant. An efficient practice, which produced no monopoly overcharge and deadweight loss at all, and an inefficient, monopolizing practice might both drive a competing firm out of business. The victim's losses might be precisely the same whether or not the practice was efficient. In one case, however, optimal damages would be zero, in the other very large.

HOVENKAMP, *supra* note 5, at 662.

[69] *See* Frank H. Easterbrook, *Predatory Strategies and Counter-Strategies*, 48 U. CHI. L. REV. 263, 331 (1981) (proposing this rule for predatory pricing cases). *See also* Frank H. Easterbrook, *On Identifying Exclusionary Conduct*, 61 NOTRE DAME L. REV. 972 (1986).

"early warning" system that likely benefits consumers in the long run.[70] In any event, courts continue to permit competitor lawsuits based on market foreclosure, and they must therefore develop means of separating the procompetitive wheat from the anticompetitive chaff.

2. HOW A FAILURE TO MITIGATE DEFENSE COULD HELP A failure to mitigate defense could assist courts with that difficult task. To see why, first consider what it means for foreclosure-causing conduct to be "anticompetitive."[71] In a genuinely competitive system, each competitor will try his hardest, and the winner will be the contestant possessing the most superior skills, e.g., the fastest runner, the highest vaulter, etc. In business competition, the winner should be the most efficient producer (recognizing that both cost and quality are elements of efficiency). If a business practice results in a "winner" who is someone other than the most efficient producer, it is inconsistent with genuine competition—in other words, it is anticompetitive. A fair starting point in defining anticompetitive conduct, then, would be Judge Posner's test for identifying "exclusionary" conduct for section 2 purposes: such conduct is that which is "likely in the circumstances to exclude from the defendant's market an equally or more efficient competitor."[72]

A number of theorists have criticized Judge Posner's test on grounds that it would not condemn practices that exclude competitors that are not currently equally efficient but would become so but

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[70] *See* Herbert Hovenkamp, *Antitrust's Protected Classes,* 88 MICH. L. REV. 1, 31 (1989).

[71] This is a hot topic in the section 2 literature, in which commentators have articulated several tests for identifying "exclusionary" conduct under section 2. *See generally* Herbert Hovenkamp, *Exclusion and the Sherman Act,* 72 U. CHI. L. REV. 147 (2005) (cataloguing tests for identifying exclusionary conduct); Elhauge, *supra* note 13, at 330 (proposing test for exclusionary conduct); Symposium, *Identifying Exclusionary Conduct under Section 2,* 73 ANTITRUST L. J. 311 (2006). The problem similarly inheres, however, in section 1 claims based on foreclosure-causing conduct, i.e., exclusive dealing and tying. Under both statutory provisions, courts' ultimate goal should be to condemn practices that deny consumers the benefit of vigorous competition, but leave alone those practices that are consistent with competition.

[72] RICHARD A. POSNER, ANTITRUST LAW 194–95 (2d ed. 2001).

for the practice at issue.[73] For example, if a bundled discount allowed the discounter to capture so much market share that its rivals could not achieve the economies of scale necessary to become as efficient as the discounter, the discount would pass muster under Judge Posner's test (the excluded rivals would be less efficient than the discounter), but might still seem troubling.[74] I have therefore argued elsewhere for a test that would deem conduct anticompetitive if it could exclude a "competitive rival," which is defined as a rival that is either as efficient as the defendant *or* would likely become so if given the opportunity to sell enough of its product to achieve the economies available at the defendant's scale of production.[75]

If we start with the assumption that foreclosure-causing conduct is anticompetitive if, but only if, it could exclude a competitive rival (as defined above), a failure to mitigate defense could assist courts in separating pro- from anticompetitive foreclosure-causing practices. The defense would identify plaintiffs whose foreclosure is not occasioned by truly anticompetitive conduct but is instead a result of either "plaintiff laziness" (i.e., plaintiff's unwillingness to compete vigorously) or "plaintiff incompetence" (i.e., plaintiff's inability to match its rival's efficiency upon attaining the efficiencies available at the rival's scale).[76]

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[73] *See, e.g.*, Elhauge, *supra* note 13, at 320–23. *See also* Hovenkamp, *supra* note 70, at 153–55 (criticizing Posner's test on other grounds).

[74] *See* LePage's, Inc. v. 3M, 324 F.3d 141, 161 (3d Cir. 2003) (en banc) ("As a result [of defendant's bundled discounts, which expanded its market share], LePage's [sic] manufacturing process became less efficient and its profit margins declined. In transparent tape manufacturing, large volume customers are essential to achieving efficiencies of scale."); Lambert, *supra* note 52, at 1712 (discussing concern that bundled discounts may preclude rivals from attaining minimum efficient scale).

[75] Lambert, *supra* note 52, at 1740. Note that the goal of protecting rivals that are as efficient as the defendant or are likely to become so if afforded the opportunity to grow is largely consistent with the various competing views on what constitutes "exclusionary" conduct for purposes of section 2 of the Sherman Act. *Id.* at 1741, n.217.

[76] There are three possible proximate causes for profit losses a competitor plaintiff experiences following the defendant's adoption of foreclosure-causing

Consider plaintiffs who make no effort to respond to defendants' adoption of foreclosure-causing practices by lowering their prices to marginal cost, searching for alternative markets, seeking to become suppliers to the defendants, or, in bundled discount cases, seeking to collaborate with other sellers to create competitive offerings. If a defendant shows that the plaintiff did not do these things and could have mitigated its profit losses by doing so, then the court may infer that the plaintiff's avoidable losses were not occasioned by the anticompetitive nature of the defendant's practices but were instead the result of the plaintiff's unwillingness to compete vigorously, i.e., of its own laziness). The court would further the policy of vigorous competition by denying recovery for the profit losses that could have been avoided had the plaintiff "tried harder."

But what about diligent plaintiffs whose foreclosure is not the result of their failure to compete vigorously but is instead occasioned by their incompetence, i.e., their inability to match the defendant's efficiency at the defendant's scale of production? A failure to mitigate defense could help courts identify those plaintiffs as well. The burden would be on the defendant to show that the plaintiff's foreclosure resulted from the fact that it was not (and could not become, producing at defendant's scale) as efficient a producer as the defendant. It would, of course, be very difficult for the defendant to offer direct proof of plaintiff's relative inefficiency; cost data are both difficult to obtain and notoriously manipulable. But the defendant likely could prove facts regarding its willingness to accept a plaintiff's supplier offer, and those facts could provide indirect proof of the plaintiff's rel-

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practices. First, some plaintiffs may simply refuse to engage in vigorous competition—they may refuse to search for alternative markets or to lower their prices from supracompetitive levels. Second, some plaintiffs may be willing to compete vigorously but may simply be incapable of matching the defendant's efficiency. For example, a plaintiff that lowers its price to marginal cost may still be excluded by a more efficient competitor. Finally, some plaintiffs may lose profits not because they are unwilling to compete vigorously or unable to match the defendant's efficiency but because the defendant's conduct confers an unfair advantage that cannot be overcome by a combination of hard work and competence. Courts adjudicating claims for foreclosure-based damages should penalize defendants to the extent plaintiff's profit loss results from the third cause, but not to the extent that it results from the first two.

ative inefficiency. Suppose, for example, that the defendant proved that it offered to purchase the competitive product from plaintiff at a price equal to defendant's marginal cost. Plaintiff's refusal to accept this offer would suggest that the price being offered was below what plaintiff's marginal cost would be if it were producing enough to supply the defendant—in other words, that plaintiff was not a competitive rival. Or the defendant might offer proof (rebuttable by plaintiff, of course) that it *would have* purchased from plaintiff at any price lower than its (defendant's) marginal cost if plaintiff had made a favorable supplier offer. Plaintiff's failure to make such an offer would suggest either (1) that it knew it was a less efficient producer than defendant, (2) that it did not exhaust all reasonable avenues for staying in the market, or (3) that it did not believe defendant would have accepted such an offer had it been extended. Defendant, of course, would attempt to prevent a factfinder from drawing the third conclusion by creating record evidence that it would have accepted a favorable supplier offer. Thus, the failure to mitigate defense would have the ex ante effect of encouraging the parties to create evidence regarding their relative efficiencies.

In sum, recognition of a failure to mitigate defense to foreclosure-based lost profits claims could help courts solve what Judge Easterbrook has called "the puzzle of exclusionary conduct"—a puzzle that exists because "competitive and exclusionary conduct look alike."[77] By focusing the evidentiary record on plaintiffs' competitive efforts and the relative efficiencies of the parties, the defense would help courts identify situations in which foreclosure occurred because of plaintiff sloth or relative inefficiency, not because the defendant's conduct was truly anticompetitive. The defense would thereby lower the error costs involved in the adjudication of foreclosure-based lost profits claims.

B. Behavior by defendants

Recognition of a failure to mitigate defense to foreclosure-based lost profits claims would also have the salutary effect of encouraging potential defendants to pursue novel, but procompetitive, marketing

[77] Easterbrook, *supra* note 67, at 345.

practices. Damage awards based on lost profits from market foreclosure can be tremendous,[78] and the standards for assessing liability are fuzzy at best.[79] Because judges—much less juries—are frequently incapable of recognizing when foreclosure-causing conduct is procompetitive, defendants are understandably reluctant to engage in novel business practices that, although output-enhancing, have the incidental effect of foreclosing competitors from marketing opportunities. Given that judicial mischaracterization of such practices could result in massive treble damages awards, businesses tend to be unduly conservative in attempting untested marketing techniques that could benefit consumers in the long run.[80]

A failure to mitigate defense could remedy this inefficient conservatism by providing safe harbors for foreclosure-causing practices that are not, on the whole, anticompetitive, i.e., that could not exclude a rival that was at least as efficient as the defendant or could become so if given the opportunity to capture the economies available at the defendant's scale of production. If failure to mitigate were recognized as a valid defense, a plaintiff that found itself foreclosed by a competitor defendant's marketing practice would be expected to mitigate its damages by offering to supply the defendant with the relevant product or service at a price equal to the plaintiff's marginal cost. If the offer price was less than or equal to the defendant's marginal cost of producing the product, the defendant could both avoid liability and reduce its costs of production (or, at worst, leave them unchanged) by accepting the offer.[81] If the offer price was greater than the defendant's marginal

[78] *See, e.g., LePage's*, 324 F.3d at 147 (upholding $68 million foreclosure-based antitrust judgment resulting from claims challenging, inter alia, bundled discounts); Gary Young, *$519 Million Antitrust Judgment: Hill-Rom Claims Verdict Will Not Stand*, NAT'L J., Oct. 2, 2002, at A9 (detailing large antitrust verdict resulting from foreclosure-based claim).

[79] *See generally* Elhauge, *supra* note 13, at 253–54 (discussing "vacuous" nature of monopolization standards used by courts).

[80] *Id.* at 266–67 (noting that "[t]hese sorts of risks cannot help but chill investments to create product offerings with a sufficient quality or cost advantage over preexisting market options to enjoy monopoly power").

[81] There could be no liability, for the plaintiff would not be foreclosed. And the defendant's costs of production would decrease by the extent of the plaintiff's efficiency advantage.

cost, the defendant could point to that fact to establish that its conduct, although foreclosure-causing, was not excluding a competitive rival and thus was not anticompetitive. A failure to mitigate defense could thereby help counter defendants' understandable conservatism toward output-enhancing marketing practices that have the incidental effect of foreclosing competitors.[82] The defense would thus reduce instances of inefficient conduct—or, more precisely, nonconduct—by defendants.

C. *Behavior by plaintiffs*

Finally, it should be obvious that recognition of a failure to mitigate defense in this context would have a salutary effect on plaintiffs' conduct. Social welfare is enhanced if plaintiffs who are foreclosed from a market redeploy their productive resources elsewhere,[83] and a failure to mitigate defense would encourage them to do so. Social welfare is further enhanced if plaintiffs who can produce a product more efficiently than their foreclosure-causing competitors take over production of the product for those competitors. The failure to mitigate defense outlined above would encourage efficient producers who found themselves foreclosed to become suppliers to their rivals.[84]

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[82] Consider a couple of examples of how the defense might work in practice. Suppose defendant, seeking to take advantage of economies of scope, offers a bundled discount on products *A*, *B*, and *C*. The discount has the incidental effect of foreclosing a business that sells product A but not products *B* and *C*. If the smaller manufacturer is required to mitigate its damages, it will seek to supply product *A* to the defendant. If the manufacturer is as efficient a producer of product *A* as the defendant, the defendant will accept the manufacturer's supplier offer and the manufacturer will not be foreclosed. If the manufacturer is less efficient, its foreclosure cannot have been anticompetitive.

Or consider a tying arrangement. Suppose defendant, seeking to meter demand for its monopoly product *A*, ties its product *B* to product *A*. Plaintiff, a small manufacturer of *B*, is foreclosed by the tie-in. If plaintiff is required to mitigate its damages, it will seek to supply product *B* to the defendant. If plaintiff is equally efficient, defendant will accept its supply offer and plaintiff will not be foreclosed. If plaintiff is less efficient, its foreclosure cannot have been anticompetitive.

[83] *See supra* notes 29–30 and accompanying text.

[84] Some might find this effect troubling, for inviting cooperation among competitors may increase the risk of collusive output reduction. *See* Verizon

VI. CONCLUSION

The oft-repeated mantra that antitrust plaintiffs have a duty to mitigate their damages is not exactly correct. Sometimes they do, and sometimes they don't. And that's the way it should be. This article has attempted to set forth a simple theory for when a mitigation duty—or, more precisely, a failure to mitigate defense—should be recognized. If the objective of the defense is to minimize social costs, which would include inefficient behavior by the parties and the administrative costs of claim adjudication, then a failure to mitigate defense should not be recognized when plaintiffs are seeking to recover overcharges but should be recognized when plaintiffs are seeking to recover lost profits—even if the claimed profit losses are a result of purported market foreclosure.

Comm'ns, Inc. v. Law Offices of Curtis V. Trinko LLP, 540 U.S. 398, 408 (2004) ("[C]ompelling negotiation between competitors may facilitate the supreme evil of antitrust: collusion"). *See generally* Christopher R. Leslie, *Trust, Distrust, and Antitrust*, 82 TEX. L. REV. 515 (2004) (arguing that a primary objective of antitrust law is, and should be, to create distrust among competitors). But as long as the supplier competitors are free to sell directly to the defendant's customers, their continued presence in the market should prevent the defendant from being able to cut its own production and raise prices above competitive levels; if it did so, its supplier rivals would increase their production and undersell it. The defendant might therefore cut a deal with rivals, offering to share its supracompetitive profits if the rivals would not undersell it. But such an agreement, which would be per se illegal, would be rather easy to identify, for output would fall, price would rise, and the seller would be unable to articulate a valid reason for its decision to cut production. *See* Lambert, *supra* note 52, at 1755–56.